FILED
AUG 20 1993
OFFICE OF THE CLERK

No. 92-1370

In The

Supreme Court of the United States

October Term, 1993

In Re: BFP, A Partnership, Debtor

BFP, A PARTNERSHIP,

Petitioner,

v.

RESOLUTION TRUST CORPORATION, AS RECEIVER FOR IMPERIAL FEDERAL SAVINGS ASSOCIATION; PAUL OSBORNE; WILLIAM LITTLE; DENNIS ROY; ARTHUR RITZ; JOSE CRUZ; RICHARD MARCZ,

Respondents.

On Writ of Certiorari
To The United States Court Of Appeals
For the Ninth Circuit

BRIEF OF CALIFORNIA TRUSTEE'S ASSOCIATION, CALIFORNIA LAND TITLE ASSOCIATION, CALIFORNIA BANKERS ASSOCIATION, THE MORTGAGE INSTITUTE OF CALIFORNIA AND CALIFORNIA INDEPENDENT MORTGAGE BROKERS ASSOCIATION AS AMICI CURIAE IN SUPPORT OF RESPONDENTS

PHILLIP M. ADLESON, ESQ.*
*Counsel of Record
PATRIC J. KELLY, ESQ.
BARBARA B. CHRISTENSEN, ESQ.
DUANE W. SHEWAGA, ESQ.
ADLESON, HESS, CHRISTENSEN & KELLY
110 North Third Street
San Jose, California 95112
(408) 297-6605
Attorneys for Amici Curiae

COCKLE LAW BRIEF PRINTING CO., (800) 225-6964
OR CALL COLLECT (402) 342-2831

BEST AVAILABLE COPY

TABLE OF CONTENTS

	Page
INTEREST OF AMICI CURIAE	1
SUMMARY OF ARGUMENT	3
ARGUMENT	4
I. The Fraudulent Conveyance Laws Have Never Been Applied to Upset Legitimate Business Transactions Nor Used To Set Aside Non-Collusive, Non-Fraudulent Foreclosure Sales of Real Property Security Interests	4
A. Introduction	4
B. Some History of the *Madrid/Durrett/Bundles* Controversy	4
C. History and Purposes of the Fraudulent Conveyance Laws	6
D. The Purpose of California Fraudulent Conveyance Law in No Way Differs from that of Bankruptcy Code § 548	7
E. Fraudulent Conveyance Laws Emanating from the Statute of 13 Elizabeth Have Sought to Correct the Actual Fraud of a Debtor and His Transferees, Establishing "Badges of Fraud" to Prove That Which Cannot Be Proved by Direct Evidence	8
II. The Nonjudicial Foreclosure Process in California	10
A. The Procedure	10
B. Nonjudicial Foreclosure in California is Created by Contract and Substantially Restricted by Statute	12

TABLE OF CONTENTS – Continued

Page

1. The Nature of the Deed of Trust..... 12

2. Notice of Default..... 12

3. Notice of Sale..... 13

4. Reinstatement and Redemption Rights..... 13

5. Costs, Expenses and Trustee's Fees... 14

6. The Sale..... 14

7. The Anti-Deficiency Statutes..... 14

C. The 9th Circuit and Congress Have Recognized That Consonance Between State Foreclosure Law and Bankruptcy Law is Critical to the Stability of Titles and the Lending Industry..... 15

III. Prior to *Durrett*, No Case in the 400 Year History of the Fraudulent Conveyance Laws Has Set Aside a Nonjudicial Foreclosure Sale in the Absence of Actual Fraud or Collusion. In the Absence of Congressional Indication to the Contrary, a Statute will not be Interpreted to Repeal a Common-Law Doctrine..... 16

IV. The Effect of the BAFJA Amendments Redefining "Transfer" and Adding "Voluntary or Involuntary" to Transfers Subject to § 548 Merely Restated What the Law Was..... 17

V. Improper Focus Has Been Placed on Perceived "Evils" of the Foreclosure Procedure. The True Focus Should Be on the Debtor and the Debtor's Obligations..... 19

TABLE OF CONTENTS – Continued

Page

VI. While Professing to Eschew Policy Concerns, *Bundles, Durrett,* and other Similar Cases Create New, Unprecedented Policy of Dubious Value and of Great Mischief..... 21

VII. BFP Amici Make Several Arguments Which Do Not Hold Up Under Scrutiny..... 23

A. BFP Amici argue that existing state foreclosure laws do not contain protections ensuring that the debtor's estate obtains appropriate value as a result of a foreclosure sale..... 23

B. Foreclosure sales are regularly advertised in such a fashion that anyone seeking to purchase at such sales can do so..... 24

C. No evidence exists that either mortgagees or bidders at foreclosure sales regularly receive windfall profits. The evidence is to the contrary..... 25

D. Mortgagees do have incentive to bid at foreclosure sales and almost never receive a double recovery in the form of a deficiency judgment..... 27

E. Competitive bidding does exist on properties with sufficient value to warrant such bidding..... 28

F. Allowing § 548 set asides will increase the cost of mortgage lending..... 28

VIII. Billions of Dollars of Second Mortgage Capital Would be Endangered Should Foreclosure Sales be Subject to Set-Aside for up to Three Years After They Occur..... 29

CONCLUSION..... 29

TABLE OF AUTHORITIES

Page

CASES

Abramson v. Lakewood Bank & Trust Co., 647 F.2d 547 (5th Cir. 1981) 7

Bundles v. Baker (In re Bundles), 856 F.2d 815 (7th Cir. 1992) ..... *passim*

Chichester v. Mason, 43 Cal.App.2d 577, 111 P.2d 362 (1941) 7

Durrett v. Washington National Ins. Co., 621 F.2d 201 (5th Cir. 1980) ..... *passim*

Ehring v. Western Community Moneycenter (In re Ehring), 900 F.2d 184 (9th Cir. 1990) 6, 18

Garfinkle v. Superior Court, 21 Cal.3d 268, 146 Cal.Rptr. 208 (1978) 10

Huene v. Cribb, 9 Cal.App. 141, 98 P. 78 (1908) 12

I.E. Associates v. Safeco Title Ins. Co., 39 Cal.3d 284, 288, 216 Cal.Rptr. 438 (1985) ..... *passim*

In re BFP, 974 F.2d 1144 (9th Cir. 1992) 6

In re Ehring, 91 B.R. 897 (9th Cir. BAP 1988) 6

In re Kachanizadeh, 108 B.R. 734 (Bankr.C.D. Cal. 1989) 5

In re Lindsay, 98 B.R. 983 (Bankr.S.D.Cal. 1989) 5, 16, 19, 20

In re Verna, 58 B.R. 246 (Bankr.C.D.Cal. 1986) 5, 22

In re Winshall Settlor's Trust, 758 F.2d 1136 (6th Cir. 1985) 8

Koch v. Briggs, 14 Cal. 256 (1859) 10

TABLE OF AUTHORITIES – Continued

Page

Kupetz v. Wolf, 845 F.2d 842 (9th Cir. 1988) ..6, 7, 15, 16

Madrid v. Lawyers Title Ins. Corp (In re Madrid), 725 F.2d 1197 (9th Cir. 1984) 4, 5, 7, 17

Madrid v. Lawyers Title Ins. Corp (In re Madrid), 21 B.R. 424 (9th Cir. BAP 1982) 4, 5, 7, 17

Schmidt v. Klipfel, 59 Cal.App.2d 197 (1943) 13

FEDERAL STATUTES

11 U.S.C. § 548 ..... *passim*

11 U.S.C. § 548(a) 21

11 U.S.C. § 548(a)(2)(A) 3, 4, 5, 8

Bankruptcy Amendments & Federal Judgeship Act of 1984, Pub. L. No. 98-353 5

STATE STATUTES

Civ. Code § 2920 12

Civ. Code § 2924 ..... 11, 13

Civ. Code § 2924b 13

Civ. Code § 2924c 13, 23

Civ. Code § 2924c(c) 14, 20, 23

Civ. Code § 2924c(d) 14, 20

TABLE OF AUTHORITIES – Continued

Page

Civ. Code § 2924c(e) 13

Civ. Code § 2924d 14, 20

Civ. Code § 2924f 13, 24

Civ. Code § 2924g 14

Civ. Code § 2924h(d) 14

Civ. Code § 3439.08(e)(2) 7, 18

Civ. Code §§ 2903-2905 13

Code of Civ. Proc. § 580a 14

Code of Civ. Proc. § 580b 14

Code of Civ. Proc. § 580d 14, 27

Code of Civ. Proc. § 726 ..... 14, 27

West's Ann.Cal.Civ.Code, 1990 Supp., § 3439.08 7

Stats. 1933, c. 642 13

OTHER AUTHORITIES

4 Collier, *Bankruptcy Practice Guide*, "Fraudulent Conveyances", par. 65.02, pages 65-3 through 65-4 8

CEB, *California Mortgage and Deed of Trust Practice* (2d Ed. 1990) "Debtor Strategies", § 6.40, pp. 319-320 ..... 11, 23

Kennedy, *Involuntary Fraudulent Transfers*, 9 Cardozo L. Rev. 531 (1987) 6

TABLE OF AUTHORITIES – Continued

Page

Osborne, *Mortgages*, (West 2d Ed. 1970) § 8 pp. 17-19 13

Shuchman, *Data on the Durrett Controversy*, 9 Cardozo L. Rev. 605 (1987) 6

Statute of 13 Elizabeth in 1571 6

Sutherland, *Statutory Construction*, (4th ed.) § 61.03, p. 190 17

Uniform Fraudulent Transfer Act 7

Wechsler, *Through the Looking Glass: Foreclosure by Sale as De Facto Strict Foreclosure – An Empirical Study of Mortgage Foreclosure and Subsequent Resale*, 70 Cornell L. Rev. 850 (1985) 27

Zinman, *Durrett Data: Shucking the Husks from the Grain*, 9 Cardozo L. Rev. 1013 (1988) 6

Zinman, *Noncollusive, Regularly Conducted Foreclosure Sales: Involuntary, Nonfraudulent Transfers*, 9 Cardozo L. Rev. 581 (1987) 6, 17, 27, 28, 30

Amici Curiae California Trustee's Association (CTA), California Land Title Association (CLTA), California Bankers Association (CBA), the Mortgage Institute of California (MI), and California Independent Mortgage Brokers Association (CIMBA) (collectively Association) respectfully submit their brief in support of respondents Resolution Trust Corporation, as receiver for Imperial Savings & Loan Association, Paul Osborne, William Little, Dennis Roy, Arthur Ritz, Jose Cruz, and Richard Marcz (Respondents) in the above-entitled appeal.

INTEREST OF AMICI CURIAE

Amicus CTA is comprised of trustees under deeds of trust secured by real property in California as well as of members working for industries which provide support services in the nonjudicial foreclosure process (e.g., legal newspapers, title companies, posting services and attorneys). CTA's members provide reconveyance and nonjudicial foreclosure services for literally all lenders in the California real estate market.

Amicus CLTA is a nonprofit corporation composed of title insurance companies and underwritten title companies doing business in California. Approximately 130 of the approximately 136 such companies doing business in California are members of CLTA. CLTA members provide title insurance and related products and frequently act as trustees under deeds of trust secured by real property.

Amicus CBA is a nonprofit corporation with over 420 member banks, representing virtually every commercial bank in California.

Amicus MI, whose current corporate membership exceeds 225 companies, is a trade association which, since 1954, has represented the interests of mortgage loan brokers and others engaged in the business of making, arranging, and servicing real estate loans in California.

Amicus CIMBA is a nonprofit California corporation which functions as a statewide trade association comprised primarily of mortgage loan brokers whose main business is arranging residential loans for private borrowers which are generally funded by other private individuals or small pension plans.

Both MI and CIMBA are members of the Real Estate Finance Advisory Committee to the California Real Estate Commissioner and each sponsors continuing education seminars approved for credit by the California Department of Real Estate. Each of the Amici Association have been actively involved in legislation and/or as amici before state and federal courts of appeal (including Supreme Courts) regarding nonjudicial foreclosure, title, title insurance, banking, mortgage brokering, and lending law.

The Association's primary interest in the Court's resolution of the instant case is that if Petitioner's position is adopted by the Court, such a result would disturb the delicate balance of rights and responsibilities between trustors, beneficiaries, and trustees established over many years by contracts and statutes enacted by the California legislature; it will impose ambiguous duties upon beneficiaries and trustees, many of the costs for such new and ambiguous duties will not be recoverable under state law; it will lead to more bankruptcies as well as more litigation regarding title and foreclosures; it will create uncertainty of title, uninsurable and unmarketable title; it will further destabilize the real estate market and lending industry, lower property values, unnecessarily increase the costs of foreclosure; it will increase the costs of borrowing; and it will reduce the availability of financing, particularly private financing, upon which the most needy consumer-borrowers rely.

SUMMARY OF ARGUMENT

The issues before the Court involve what has been commonly referred to as the *Madrid/Durrett/Bundles* controversy. That is, whether or not 11 U.S.C. § 548(a)(2)(A) (the constructively, fraudulent conveyance section of the Bankruptcy Code) can be used to set aside a regularly conducted, non-collusive nonjudicial foreclosure sale. The fraudulent conveyance laws, before *Durrett*, have never been used to set aside non-collusive, regularly conducted nonjudicial foreclosure sales as these laws were never intended to apply to such sales.

Consonance between state foreclosure laws and bankruptcy law is critical to the stability of titles and the lending industry.

Foreclosure is not an "evil" procedure. It is a necessary step in the real property lending process to assure that losses to lenders are minimized. Without security and foreclosures on defaulted loans, there would be no lending industry. The true focus should be on owners who fail to market their properties when it is clear that the property cannot be retained.

State foreclosure laws, at least in California, are protective of all parties to the transaction. Applying the bankruptcy laws to effect a federal right of redemption, heretofore unheard of, would drive down bidding on properties and result in fewer lenders in the market, particularly secondary lenders. To the detriment of the consumer-borrower, the cost of borrowing will increase, the ease of borrowing or availability of funds will decrease, and the state of post-foreclosure title will become uncertain and uninsurable reducing the ability to resell properties after foreclosure at their fair market value. The fear of having an investment tied up for up to three years after a foreclosure sale will send private (often junior) lenders into other investments.

ARGUMENT

I. The Fraudulent Conveyance Laws Have Never Been Applied to Upset Legitimate Business Transactions Nor Used To Set Aside Non-Collusive, Non-Fraudulent Foreclosure Sales of Real Property Security Interests.

A. Introduction.

The questions before the Court involve the *Madrid/Durrett/Bundles* debate[1] and the imposition of either a "percentage of fair market value" and/or a fact-specific standard on state-controlled foreclosure sales in evaluating "reasonably equivalent value" under 11 U.S.C. § 548(a)(2)(A). Association strongly disagrees with the conclusions found in *Durrett* and *Bundles* which could cripple an entire industry, render titles unmarketable for years, increase the cost of borrowing to the consuming public, reduce the availability of loan funds particularly to those most in need of loans, invite litigation in every foreclosure proceeding, and encourage bankruptcy filings in an effort to enforce a federally created right of redemption which has never before existed.

B. Some History of the *Madrid/Durrett/Bundles* Controversy.

Madrid (BAP) held that a non-collusive, regularly conducted foreclosure sale ("valid foreclosure sale")

---

[1] The two *Madrid* opinions will be referred to as *Madrid* (BAP) signifying the case of *Madrid v. Lawyers Title Ins. Corp.* (*In re Madrid*), 21 B.R. 424 (9th Cir. BAP 1982); *Madrid* (9th Cir.) signifying the case of *Madrid v. Lawyers Title Ins. Corp.* (*In re Madrid*), 725 F.2d 1197 (9th Cir. 1984), cert. denied, 469 U.S. 833 (1984); *Durrett v. Washington National Ins. Co.*, 621 F.2d 201 (5th Cir. 1980) will be referred to as *Durrett*; *Bundles v. Baker* (*In re Bundles*), 856 F.2d 815 (7th Cir. 1992) will be referred to as *Bundles*.

constituted "reasonably equivalent value" for purposes of 11 U.S.C. § 548(a)(2)(A)[2]. *Madrid* (9th Cir.) affirmed *Madrid* (BAP), but on the ground that a foreclosure sale is not a "transfer" for purposes of § 548. *Durrett* held that a foreclosure sale constituted a transfer under § 548 and could be attacked as a fraudulent conveyance if the proceeds were less than "reasonably equivalent value" as measured by the fair market value of the property. *Bundles* created a fact-specific inquiry, requiring a determination of whether an appraisal was obtained, whether there was competitive bidding, and whether the sale was widely advertised. Deference was to be given to the state foreclosure proceedings, if possible. (*Bundles* at 824, 825.) BAFJA[3] amended the definition of "transfer" to include foreclosure of the debtor's equity of redemption and to make it clear that § 548 applied to involuntary transfers.

Included in the legal debate is the effect of the BAFJA amendments; whether *Durrett* was codified; whether *Madrid* (9th Cir.) was overruled; whether *Madrid* (BAP) was left intact regarding "reasonably equivalent value"; and, whether the amendments changed anything at all.

Among the lower court cases in the 9th Circuit that have addressed the issues are:

(1) *In re Lindsay*, 98 B.R. 983 (Bankr.S.D.Cal. 1989);

(2) *In re Verna*, 58 B.R. 246 (Bankr.C.D.Cal.1986);

(3) *In re Kachanizadeh*, 108 B.R. 734 (Bankr.C.D.Cal. 1989);

---

[2] All references will be to Title 11, United States Code, unless otherwise specifically indicated. References to the "Civil Code" or to "Civ. Code" are to the California Civil Code. References to the Code of Civ. Proc. or Code of Civil Procedure are to the California Code of Civil Procedure.

[3] BAFJA refers to the Bankruptcy Amendments & Federal Judgeship Act of 1984, Pub. L. No. 98-353.

(4) *In re Ehring*, 91 B.R. 897 (9th Cir. BAP 1988), herein, *Ehring* (BAP);

(5) *Ehring v. Western Community Moneycenter*, (*In re Ehring*) 900 F.2d 184 (9th Cir. 1990), herein, *Ehring* (9th Cir.);

(6) *In re BFP*, 974 F.2d 1144 (9th Cir. 1992), herein, *In re BFP* (9th Cir.).

The issues before the Court have been the subject of an ongoing legal debate in the form of a series of law review articles from Professor Robert M. Zinman, Professor Frank R. Kennedy, and Professor Philip Shuchman.[4] The articles address both sides of the controversy now before the Court and include controverted statistical evidence regarding the impact of *Durrett*.

Following is a brief history and statement of the purpose of fraudulent conveyance laws, a description of nonjudicial foreclosures in California, and the effect of the cases and legislation since *Durrett*.

C. History and Purposes of the Fraudulent Conveyance Laws.

Fraudulent conveyance statutes, which date back to before the Statute of 13 Elizabeth in 1571, have all been intended to prohibit transfers that hinder, delay, or defraud creditors (*Kupetz v. Wolf*, 845 F.2d 842, 846 (9th Cir. 1988)), not to upset legitimate, above-board business transactions. (*Id.* at page 848.)

---

[4] The articles are: Kennedy, *Involuntary Fraudulent Transfers*, 9 Cardozo L. Rev. 531 (1987), (herein, Kennedy); Zinman, *Noncollusive, Regularly Conducted Foreclosure Sales: Involuntary, Nonfraudulent Transfers*, 9 Cardozo L. Rev. 581 (1987), (herein, Zinman); Shuchman, *Data on the Durrett Controversy*, 9 Cardozo L. Rev. 605 (1987), (herein, Shuchman Data); and, Zinman, *Durrett Data: Shucking the Husks from the Grain*, 9 Cardozo L. Rev. 1013 (1988), (herein, Zinman Data).

D. The Purpose of California Fraudulent Conveyance Law in No Way Differs from that of Bankruptcy Code § 548.

Section 548 and the California fraudulent conveyance laws have the same purpose. (*Kupetz v. Wolf*, 845 F.2d 842, 845 (9th Cir. 1988).) The purpose of California's law is to prevent debtors from placing property beyond the reach of their creditors when such property should legitimately be available for satisfaction of creditors' demands. (*Chichester v. Mason*, 43 Cal.App.2d 577, 584, 111 P.2d 362 (1941).) California's law explicitly exempts non-collusive enforcement of a lien from the fraudulent conveyance statutes. (Civ. Code § 3439.08(e)(2).) The "Legislative Committee Comment – Assembly" [West's Ann.Cal.Civ. Code, 1990 Supp., § 3439.08] on the 1986 addition to California's version of the Uniform Fraudulent Transfer Act states:

"Paragraph (2) of subdivision (e) rejects the rule of such cases as *Durrett v. Washington Nat. Ins. Co.*, 621 F.2d 201 (5th Cir. 1980) (nonjudicial foreclosure of a mortgage avoided as a fraudulent transfer when the property of an insolvent mortgagor was sold for less than 70% of its fair value); and *Abramson v. Lakewood Bank & Trust Co.*, 647 F.2d 547 (5th Cir. 1981), cert. denied, 454 U.S. 1164 (1982) (nonjudicial foreclosure held to be fraudulent transfer if made without fair consideration). Paragraph (2) of subdivision (e) adopts the view taken in *Lawyers Title Ins. Corp. v. Madrid* (*In re Madrid*), 21 B.R. 424 (B.A.P. 9th Cir. 1982), aff'd on another ground, 725 F.2d 1197 (9th Cir. 1984), that the price bid at a public foreclosure sale determines the fair value of the property sold . . . The premise of the paragraph is that 'a sale of the collateral by the secured party as the normal consequence of default

> . . . [is] the safest way of establishing the fair value of the collateral. . . . ' [cite omitted]."

The 6th Circuit agrees that reasonable equivalence for the purposes of a foreclosure sale under § 548(a)(2)(A) should be consonant with the state law of fraudulent conveyances. (*In re Winshall Settlor's Trust*, 758 F.2d 1136, 1139 (6th Cir. 1985).)

E. Fraudulent Conveyance Laws Emanating from the Statute of 13 Elizabeth Have Sought to Correct the Actual Fraud of a Debtor and His Transferees, Establishing "Badges of Fraud" to Prove That Which Cannot Be Proved by Direct Evidence.

Fraudulent conveyance statutes were enacted to prevent dubious, fraudulent activities of the debtor and were never intended to overturn a debtor's legitimate business activities. A succinct summary of the laws and their purposes is found in 4 Collier, *Bankruptcy Practice Guide*, "Fraudulent Conveyances", par. 65.02, pages 65-3 through 65-4:

> "The origin of modern fraudulent conveyance laws can be traced directly back through the development of the common law to the Statute of 13 Elizabeth, passed by Parliament in 1570. This heritage indicates that the values which the fraudulent conveyance laws are designed to vindicate are absolutely fundamental to, indeed the very keystone of, the Anglo-American approach to debtor-creditor relations. Those values are easily summarized: A person or entity with debts is not free to deal with his property in a manner which substantially increases the risk of non-payment to creditors. The unacceptable result may be manifested either through transfers of existing property rights, whether direct or indirect, complete or partial, secret or public,

> or by the assumption of obligations which do not result in a concomitant benefit to the debtor and therefore to his creditors. *These principles do not interfere with the debtor's legitimate operation of his business or conduct of his affairs; they only demand that he be reasonably compensated for the value he gives.* They examine the totality of assets convertible into cash and available to creditors for the repayment of these obligations, before and after the dubious transaction. To the extent of the prejudice to creditors the transaction may be voidable, subject to the intervening rights of innocent third parties.
>
> The fraudulent conveyance laws in most of their manifestations *do not relate to a creditor's right or ability to look to a particular asset for repayment. Rather, the principles are designed to assure that the creditor body has available for repayment a totality of value which the debtor had, or led the creditor body to believe he had, before the questionable transaction."* [emphasis added].

This summary highlights the folly of applying the statutes to a valid foreclosure sale. A lender who gives a debtor money in exchange for a promissory note equal to the loan which is secured by a deed on the debtor's property has voluntarily bargained his position with the debtor: He may collect his debt from the assets of the debtor which are secured. The collection procedure entails the sale of the assets via a statutorily regulated process. Thereafter, the "totality of value" which the "creditor body" can look to for repayment of the "body's" unsecured loan includes the equity which the debtor may have in the secured assets, but subject to the right of the secured creditor to force the sale of that property in satisfaction of the secured creditor's loan. Accordingly, the "totality of value" is measured by the asset encumbered by the danger that it may be eliminated

from the creditor's reach by foreclosure sale. The debtor's only rights in the property are equitable title, right of possession, and right of redemption. No unsecured creditor can claim to be defrauded by this transaction. He is deemed to know the consequences of the transaction by virtue of the public recording statutes and the law of foreclosures. He allows himself to become an unsecured creditor of such a debtor with his eyes open. His alternative is to not deal with the debtor or, if possible, to become secured himself. California statutes make it clear that such a transaction is not a "fraudulent conveyance". There is nothing in the Bankruptcy Code which prevents a similar conclusion, i.e., the Bankruptcy Code should be interpreted in light of past precedent and in harmony with state statutes from which the federal rule is drawn.

II. The Nonjudicial Foreclosure Process in California.

Since this matter arose in California, it is appropriate to review California's foreclosure process.

A. The Procedure.

Nonjudicial foreclosure in California has existed since the early days of statehood and has long been recognized as an efficient, expedient, and appropriate means of realizing upon real property security in the event of default by the borrower. (*Koch v. Briggs*, 14 Cal. 256 (1859).) California courts have consistently upheld the process as an appropriate and integral part of the real property security law. (*Garfinkle v. Superior Court*, 21 Cal.3d 268, 146 Cal.Rptr. 208 (1978).)

State law statutes and court opinions have carefully balanced the rights of the borrower, the lender, and of the trustee under the deed of trust. (*I.E. Associates v. Safeco Title Ins. Co.*, 39 Cal.3d 284, 288, 216 Cal.Rptr. 438 (1985).)

Procedurally deficient, fraudulent, or collusive foreclosure sales are strictly scrutinized and can be set aside under California law. (CEB, *California Mortgage and Deed of Trust Practice*, (2d Ed. 1990) "Debtor Strategies", § 6.40, pp. 319-320, herein, "CEB Mortgage Practice".) The fact that the amount bid is less than the property's market value, however, is not a sufficient ground to set aside the sale in the absence of fraud, unfairness, or oppression. (*Id.*, at p. 320.) A gross disparity between price and value empowers the court to set aside the sale if there is any evidence of unfairness or irregularity. (*Id.* at p. 320.)

Where the terms of the power of sale in the deed of trust and of the applicable statutes have been complied with, a non-collusive, nonjudicial foreclosure sale, untainted by fraud, is conclusive and cannot be set aside. (See, Civ. Code § 2924.) The rights and powers of trustees in nonjudicial foreclosures have long been regarded as strictly limited and defined by the contract of the parties and by the statutes. (*I.E. Associates, supra*, at p. 287.) The clear and important policy of the State of California, as enunciated by the California Supreme Court in *I.E. Associates, supra*, p. 288, (and most of the other western states which employ the deed of trust concept), is as follows:

> "In short, there is no authority for the proposition that a trustee under a deed of trust owes any duties with respect to exercise of the power of sale beyond those specified in the deed and the statutes. There are, moreover, persuasive policy reasons which militate against a judicial expansion of those duties. *The nonjudicial foreclosure statutes – an alternative to judicial foreclosure – reflect a carefully crafted balancing of the interests of beneficiaries, trustors, and trustees.* Beneficiaries, of course, want quick and inexpensive recovery of amounts due under promissory notes in default. Trustors, on the other hand, need protection against the forfeiture of valuable property rights. Trustees, the middlemen,

need to have clearly defined responsibilities to enable them to discharge their duties efficiently and to avoid embroiling the parties in time-consuming and costly litigation. In taking all of these concerns into account, the statutes strike an overall balance favoring the protection of trustors." [cites omitted; emphasis added].

B. Nonjudicial Foreclosure in California is Created by Contract and Substantially Restricted by Statute.

Nonjudicial foreclosure is only permitted in California where the security document (e.g. deed of trust) contains an express "power of sale" authorizing such a procedure. (*Huene v. Cribb*, 9 Cal.App. 141, 98 P. 78 (1908); and Civ. Code §§ 2920 et seq.) The contractual power of sale is restricted by numerous statutes. (*Id.*) The statutes and the deed of trust form the exclusive source of the parties' rights, duties, and liabilities. (*I.E. Associates, supra*, at pp. 285-288.) A brief outline of the scheme of regulation will show just how the California legislature has attempted to balance the rights, responsibilities, and risks between the parties to a real property secured transaction.

1. The Nature of the Deed of Trust. The deed of trust is a three-part instrument whereby the trustor conveys legal title to the trustee for the benefit of the beneficiary to secure an obligation owed by the trustor to the beneficiary.[5]

2. Notice of Default. To initiate a nonjudicial foreclosure upon default, the trustee, beneficiary, or other

---

[5] Although the deed of trust is the most frequently used real property security device in California, any security instrument with a power of sale may be foreclosed nonjudicially. (Civ. Code § 2920).

authorized person must first record and mail a notice of default to the borrower (trustor) and to certain other persons entitled to notice (e.g., beneficiaries of junior deeds of trust.) (Civ. Code §§ 2924, 2924b.) The content and form of the notice is set forth by statute. (Civ. Code §§ 2924b & 2924c.) The persons to whom such notices of default are to be sent, the method, and timing of mailing are all set forth in detail in the Civil Code. (*Id.*)

3. Notice of Sale. Before a nonjudicial foreclosure may take place, a minimum of three months must pass after the recording of the notice of default. (Civ. Code § 2924). Thereafter, a notice of trustee's sale must be published once a week for three weeks, posted on the property and in a conspicuous public place, recorded, and mailed to the same persons who were entitled to receive notice of default. (Civ. Code §§ 2924b, 2924f.)

4. Reinstatement and Redemption Rights. Many common-law jurisdictions, including California, have adopted the "equity of redemption" by statute as well as statutory rights to redeem prior to the foreclosure sale. (Civ. Code §§ 2903-2905, § 2924c; Osborne, *Mortgages*, (West 2d Ed. 1970) § 8 pp. 17-19.)

Civil Code § 2924c (i.e., the cure provision) is but one provision in a series of statutes added during the Great Depression as a mortgage foreclosure moratorium law. The purpose of these moratorium statutes was to alter the contractual rights between the debtor and the creditor to provide extensions of time and to give the debtor an opportunity to cure his default if done within a designated reinstatement period. (See, *Schmidt v. Klipfel*, 59 Cal.App.2d 197, 200-202 (1943); stats. 1933, c. 642; Civ. Code § 2924c(e).) The right to reinstate may now be made at any time within the period from recordation of the notice of default until five business days prior to the date of the trustee's sale. (Civ. Code § 2924c(e).)

5. Costs, Expenses and Trustee's Fees. Foreclosure trustee's fees, costs, and expenses which can be charged in a nonjudicial foreclosure are strictly limited by statute. (Civ. Code §§ 2924c(c)&(d) and 2924d.)

6. The Sale. The Civil Code specifies the time and place for nonjudicial foreclosures; who may postpone, under what circumstances, and how postponements are declared; the order of sale of multiple parcels absent contrary authority in the deed of trust; and how to handle sales of property located in more than one county. (Civ. Code §§ 2924g and 2924h(d).)

7. The Anti-Deficiency Statutes. California's anti-deficiency statutes minimize the likelihood of any post foreclosure personal liability for the borrower. (Code of Civ. Proc. §§ 726, 580a, 580b and 580d.) The thrust of California's anti-deficiency provisions are several fold: a) if the creditor wants an economical and quick (minimum of 111 days) resort to the security via nonjudicial foreclosure, he must eschew a deficiency altogether (Code of Civ. Proc. § 580d); b) if the creditor seeks a deficiency judgment, the creditor must use the more cumbersome, time consuming, and expensive judicial foreclosure process (Code of Civ. Proc. § 726); and, c) a deficiency may not be obtained where the deed of trust is purchase money regardless of whether judicial or nonjudicial foreclosure is utilized. (Code of Civ. Proc. § 580b.) Even in the rare instance where a deficiency judgment can be obtained, it would be limited to the difference between the debt and the "fair value" of the property as determined by the court in a fair value hearing. This encourages the creditor to bid up the property to its fair value as that amount will be a floor used in determining any potential deficiency.

The California nonjudicial foreclosure system has long been recognized as a balanced system which, on the

whole, functions well for all parties to the secured real property transaction. The California courts have left the imposition of new and additional requirements relating to the nonjudicial foreclosure of deeds of trust to the Legislature. (*I.E. Associates, supra,* at pp. 288-289.)

C. The 9th Circuit and Congress Have Recognized That Consonance Between State Foreclosure Law and Bankruptcy Law is Critical to the Stability of Titles and the Lending Industry.

Bankruptcy law, as developed over recent years in the 9th Circuit and in Congress, has recognized the importance of the state's nonjudicial foreclosure process, its place in the real property security scheme, and the need for continuing its stability and the stability of land titles.

Based upon the foregoing recognition, a valid foreclosure sale cannot be set aside, under the better reasoned bankruptcy law decisions. In balancing the purposes of the nonjudicial foreclosure process with the purposes of the fraudulent conveyance law, an attack on a foreclosure sale under § 548 cannot stand. It is appropriate to balance the policy concerns behind the issues facing the Court.

The Bankruptcy Code is not so clear on its face that policy concerns cannot be taken into account. For example, in *Kupetz, supra,* the 9th Circuit makes it clear that § 548 is not to be applied to legitimate business transactions that may technically fall within its parameters. (*Id.*, at p. 847.) While the court recognized that lack of fraudulent intent does not bar a fraudulent conveyance claim, it declined to utilize constructive intent to frustrate the purposes intended to be served by the legitimate business transaction before it. (*Id.*, at p. 848.)

Similarly, this case involves a legitimate secured lender/borrower transaction. There is no hint of fraud,

collusion or improper practices. Accordingly, it is difficult to rationalize why this legitimate business transaction, above board and of public record, should be set aside as a fraudulent conveyance. (See, *Kupetz* at p. 849, fn. 16.) Many courts have recognized the importance of the stability of titles and the detrimental economic effect of applying the fraudulent conveyance law to the foreclosure statutes. (See, *In re Lindsay, supra,* at p. 989, fn. 7.) While *Lindsay* cites Shuchman Data for statistics contrary to the concerns found in the footnote cases, the Zinman Data article throws considerable doubt on the Shuchman Data study and is not cited in *Lindsay*.

III. Prior to *Durrett*, No Case in the 400 Year History of the Fraudulent Conveyance Laws Has Set Aside a Nonjudicial Foreclosure Sale in the Absence of Actual Fraud or Collusion. In the Absence of Congressional Indication to the Contrary, a Statute will not be Interpreted to Repeal a Common-Law Doctrine.

One of the most interesting statements in Zinman, at page 584, is his response to Professor Kennedy's conclusion that applying the fraudulent conveyance law to valid foreclosure sales is "not so novel." Professor Zinman replies that "[n]one of the cited cases overturning foreclosures deals with valid foreclosure sales. [fn. 19]. The cases involving foreclosure sales cited by Professor Kennedy . . . invariably disclosed some kind of collusion." In fact, Zinman states:

> "The point, of course, is that the concept of intent was not being read out of the statute. On the contrary, the purpose of the badges, presumptions, and finally the constructive fraud provisions was to develop methods of ferreting out those transactions that are inequitable to creditors by the debtor's deliberate design or

> indifference. *Noncollusive*, regularly conducted foreclosure sales, nonfraudulent by definition, were not within the 'mischief' for which the statute was written, and thus, until *Durrett*, courts did not apply fraudulent conveyance laws to these sales."

(Zinman, at p. 584.) As a matter of statutory interpretation, when there is no indication that Congress intended to abolish a well-established common-law doctrine through the passage of a statute, the act will be interpreted in a way that will preserve the common-law doctrine. (Sutherland, *Statutory Construction*, (4th ed.) § 61.03, p. 190.) For the purpose of this rule, "common law" should be understood to carry its broadest meaning of the existing body of law, rather than the narrower definition of an ancient body of Anglo-American judge-made principles. (*Id.*, § 61.01, p. 173.)

The plain result should be here, as it has been in the 9th Circuit both before and since *Madrid* (BAP), that there is no fraudulent conveyance in a valid foreclosure sale under state law. Such sales simply do not come within the purview of the statute.

IV. The Effect of the BAFJA Amendments Redefining "Transfer" and Adding "Voluntary or Involuntary" to Transfers Subject to § 548 Merely Restated What the Law Was.

Zinman states, and Kennedy agrees, that the effect of BAJFA was to restate the law as it then existed. (Zinman, p. 582.) "Thus, the amendments were effective only in overcoming the more extreme voices claiming that a foreclosure was not a transfer at all for the purposes of section 548". (*Id.*) Zinman is recognizing that *Madrid* (9th Cir.) went too far when it held that a foreclosure sale did not constitute a transfer. Clearly, a foreclosure sale does constitute a transfer of an owner/debtor's interest in real

property.[6] However, Professor Zinman makes it clear that the BAFJA **DID NOT** change decisions holding that valid foreclosure sales constitute reasonably equivalent value. (*Id.*, pp. 582-583.) (See, also, the Uniform Fraudulent Transfer Act which so provides and Civ. Code § 3439.08(e)(2).)

BAFJA should only be construed as giving a bankruptcy trustee the power to set aside foreclosure sales which are otherwise infirm. A devious debtor could conjure up a fraudulent deed of trust with the purpose of allowing the property to be foreclosed and transferred to a conspiring beneficiary. This type of transaction could be set aside under § 548. The need to have foreclosure included in the definition of transfer is obvious for this purpose. However, there is no need to read into the amendments an intention to invalidate legitimate loan transactions under the definition of "fraudulent conveyance".

Petitioner and its advocates claim that § 548 must be interpreted according to its plain meaning and its purpose, asserting that there is no exception in § 548 for valid foreclosure sales. They define § 548's purpose as: 1) giving the debtor a fresh start; 2) giving effect to the trustee's power to avoid; and 3) providing for the equitable distribution of the debtor's estate to all creditors. (BFP Amici, p. 8.) Respectfully, petitioner and BFP Amici are incorrect in their statements. The purpose of § 548 is to allow the trustee to avoid the debtor's transfers which have historically been suspect and fraudulent, thereby undoing the debtor's transactions which remove assets

---

[6] The "interest", however, is limited to the debtor's right of redemption, equitable title and right to possession. *Ehring* (9th Cir.) at pp. 187-188.

from the "creditor body's" reach. Its purpose is not to upset legitimate business transactions.

Section 548 cannot be interpreted in a vacuum. There is a long and revered history of the statute as interpreted in both state and federal case law. This history cannot be ignored in determining whether valid foreclosure sales can be set aside.

V. Improper Focus Has Been Placed on Perceived "Evils" of the Foreclosure Procedure. The True Focus Should Be on the Debtor and the Debtor's Obligations.

The foreclosure laws of the states have been developed locally with local priorities, values, and enforcement procedures in mind. Those who propose using the fraudulent conveyance statutes to attack state foreclosure processes (never before done in history) are really seeking to impose a nationwide foreclosure system with a federally imposed right of redemption. Unsuccessful in their agenda at the state level, these advocates wish to bypass the long history of comity between state and federal law and impose procedures on state foreclosures which would have to be followed to make foreclosure sales firm under federal bankruptcy laws.

These advocates would "bring far more cost and uncertainty into the system". (*I.E. Associates, supra.*) They would impose their "policy" of "commercially reasonable" procedures on the nonjudicial foreclosure process. (*Lindsay, supra,* and *Bundles, supra.*) They would require an appraisal of the security at the time of the foreclosure, unspecified steps to encourage more bidding, and additional advertising beyond that required by state law. (*Bundles, supra,* at p. 824.) Certainly, "litigation would be likely any time a person" felt that the steps taken in the foreclosure process in attempting to be "commercially

reasonable" were insufficient, "since one could always argue that the steps taken were insufficient". (*I.E. Associates, supra*, at p. 288-299.) Such extra cost and services are not recoverable by trustees and beneficiaries under California law thereby disturbing the carefully crafted balance established by the California legislature. (Civ. Code §§ 2924c(c)&(d) and 2924d.)

On the contrary, compliance with the existing statutes mandates a valid and final foreclosure sale. All parties know their rights, duties, and liabilities under the statutes. There is no way to engraft the "commercially reasonable" procedures standard of *Bundles* and *Lindsay* or the "70% rule" of *Durrett* on to the California nonjudicial foreclosure scheme. These cases leave the hows, whos, wheres and whys unanswered. For example, there is a failure to set forth how the parties are to be compensated for these efforts and additional costs. In California, trustee's fees and costs are strictly regulated and limited by statute. (Civ. Code § 2924c(d).) Who is to pay for the advertising, the appraisal, and the steps to encourage "competitive bidding" over and above those steps set out in the statute? How is it possible to determine the "70% rule" when appraisal is an art, not a science, particularly in commercial properties where appraisals can vary widely? (Zinman, at p. 594-595.)

Finally, these advocates do not explain why the nonjudicial foreclosure process is to blame for the perceived ills, when the trustor, the one with the most to lose, should be undertaking "commercially reasonable" efforts to sell or refinance the property. If the owner cannot take these steps in a timely fashion, why should an innocent lender or trustee be required to do so when that was not part of the contractual bargain?

VI. While Professing to Eschew Policy Concerns, *Bundles, Durrett,* and other Similar Cases Create New, Unprecedented Policy of Dubious Value and of Great Mischief.

The adverse results of adopting the *Bundles* or *Durrett* standard in addition to the already existing statutory foreclosure procedures are monumental, but include:

1. the difficulty, if not impossibility, in obtaining marketable and insurable title following a foreclosure sale;

2. the long statute of limitations to which a foreclosed property would be subject, thus rendering title unstable for years; [one year (§ 548(a)) plus two years after a bankruptcy is filed (§ 546(a))];

3. the uncertainties and increased, uncompensable costs in the foreclosure process, decreasing or eliminating the viability of the foreclosure trustee business, and pushing many private (i.e., "mom and pop") lenders, often the lenders of last resort to troubled debtors, out of the market;

4. the encouragement of bankruptcy filings to obtain a heretofore unheard-of nonjudicial foreclosure redemption right;

5. the reduced competitive bidding at foreclosure sales, actually reducing or eliminating overbids and any possible recovery for the debtor, junior lienholder, and/or the bankruptcy estate;

6. the long and expensive litigation over the inherently uncertain standards proposed by *Bundles*.

Bundles would require parties enforcing their real property security interest: (1) to obtain an appraisal of the property; (2) to advertise the property widely beyond that required by state law.

Chief among the Association's many concerns is that none of these efforts can be shown to actually encourage

bidding at a sale. The only real result from such efforts, besides raising nonjudicial foreclosure costs, will be to increase bankruptcy filings and litigation over what efforts were (or should have been) taken.

Parties who bid at foreclosure sales provide a valuable service to the trustor, the beneficiary, and the secured lending industry in general. (*In re Verna, supra.*) There are many publications which are subscribed to by parties interested in bidding at foreclosure sales which summarize notices of default and notices of trustee's sales from the recording offices and circulate them to their subscribers. There already exists a product to advertise foreclosure sales to those parties who are truly interested in such sales and who have the ability to purchase. It is not necessary to require further advertising.

With regard to advertising the property widely, it is inconceivable that an owner of property with any equity has not taken some steps to either refinance the obligation and/or to voluntarily market his property before it is lost to foreclosure. Real estate brokers often circulate the properties to other brokers and to the public, either via the Multiple Listing Service or through other advertisement. In addition, the trustor has an advantage in marketing his property that the beneficiary and foreclosure trustee do not have; that is, the ability to provide ready access to the property and to sell the property on terms other than all cash. If a property with any real equity cannot be sold through the customary, voluntary listing, and marketing process, it is unclear how further advertising a sale at which all cash is required to bid can bring any more bidders. Again, such a requirement would do little, if anything, to generate bidders at foreclosure sales.

Further, as indicated by the California Supreme Court in *I.E. Associates, supra,* the efficacy of the system supports striking the balance in favor of requiring the

trustor to take the steps now imposed by *Bundles*. There is no reason why the secured lender should be so burdened with uncompensable costs, fees, and expenses.

Among other of the concerns of Association are the following:

1. Who is to pay for these efforts? The trustee? The beneficiary? The trustor? The California Civil Code does not allow a beneficiary or trustee to collect charges for such additional costs. (Civ. Code § 2924c(c).)

2. What possible benefit is an appraisal of the property? How does that add to increasing the bidding at a foreclosure sale? How is a trustee or beneficiary supposed to gain access to the property to prepare a valid appraisal? Who is responsible for giving any information contained in an appraisal to a third party bidder if the information is incorrect? Foreclosure sales as they stand now are "as is, where is" as to both title and physical condition. (CEB, *Mortgage Practice,* § 2.23, p. 82; see, Civ. Code § 2924h(g).)

Balancing the results which could be achieved from the efforts required by *Bundles* and *Durrett* with the monumental problems created by such a requirement leaves little doubt that these decisions should not be followed.

VII. BFP Amici make several arguments which do not hold up under scrutiny.

A. BFP Amici argue that existing state foreclosure laws do not contain protections ensuring that the debtor's estate obtains appropriate value as a result of a foreclosure sale.

BFP Amici argue that state foreclosure procedures do not contain protections which would ensure that the debtor's bankruptcy estate will obtain value for foreclosed property. (BFP Amici, p. 41.) Firstly, it is not the

purpose of § 548 to generate value for the debtor's estate. Its purpose is to undo fraudulent transactions which put valuable assets out of the reach of legitimate creditors. Secondly, it is not the purpose of security interests and foreclosure laws to generate value for the debtor. The purpose is to pay back the secured lender for value given to the debtor. It is the debtor's job to sell the property to realize equity. If the debtor is in financial distress, the property should be sold. Any realizable equity can be recovered far more easily by the debtor in a sale listed with a real estate broker and actively marketed than in any foreclosure proceeding regardless of how the foreclosure laws are written. Again, what the BFP advocates are seeking is to judicially legislate federal foreclosure laws and a federal right of redemption under state foreclosure laws and to unify procedures the states must follow in order to allow their citizens to realize upon their bargained for security. This is not the job of the federal courts or government.

B. Foreclosure sales are regularly advertised in such a fashion that anyone seeking to purchase at such sales can do so.

BFP Amici argue that foreclosure sales are rarely advertised in a manner designed to attract bidders because the mortgagee is usually only required to advertise in legal columns of local newspapers. (BFP Amici, p. 44.) These legal columns usually consist of several columns of advertisements as opposed to regular ads for properties which may only consist of several lines. Anyone seeking to buy such properties has adequate notice of the sale. California requires publication once a week for three weeks before a sale can occur. (Civ. Code § 2924f.)

C. No evidence exists that either mortgagees or bidders at foreclosure sales regularly receive windfall profits. The evidence is to the contrary.

BFP Amici argue that only a small group of speculators appear at foreclosure sales and purchase the properties for very low prices, that lack of active competitive bidding frequently results in purchase of the property by the foreclosing mortgagee at a nominal price, and the bidding results in a windfall to the bidders. (BFP Amici, p. 45.) Such claims are not supported by the empirical evidence. On the contrary:

> "The results of the empirical study, however, do not support Professor Kennedy's windfall theory. Indeed, the results show that the mortgagee suffers a loss on resale of foreclosed properties generally, and especially in connection with the resale of commercial properties. (fn 67: The results [of the study] showed, inter alia, that all resales of foreclosed properties, both residential and commercial, produced an average loss of almost $14,000 per property. Almost half the cases involved "profits" of between $2,000 and $10,000 (over 70% of which were single-family homes, which means that losses on commercial properties were greater than the average) and half involved losses of between $2,000 and $15,000. The mortgagee was made whole in only 44% of the cases. Actually these figures do not reveal the true extent of the mortgagee's loss because profit was determined by comparing the total amount due the mortgagee on foreclosure with the resale price. Apparently not included were lost opportunity costs, maintenance expenses, repairs, brokers' fees, etc., all of which will increase the mortgagee's loss.

"The survey also revealed that third parties bought at foreclosure sales about 25% of the time, a larger percentage than critics have suggested. They found several indications that third parties bought the best properties, 'leaving the abused or neglected properties for mortgagees to purchase.' *Id.* Additionally, they concluded that local 'bank officials and their counsel, who work with mortgage foreclosures and the management and resale of properties acquired in foreclosure, appear to sincerely believe that 'lenders always lose in foreclosures.' This may be because, when taken as a group, losses do outweigh gains. . . .

"The results of the study make sense. Why would an owner with the slightest degree of sophistication allow commercial property to go into a foreclosure sale if the value of the property exceeds the amount of the mortgage? The value of real estate is what a person will pay for it, and if an owner of commercial property in financial difficulties knows there is substantial equity in the property, the owner will sell the property and realize upon that equity long before foreclosure.

"That a commercial property goes into foreclosure and is sold at a foreclosure sale for no more than the mortgage balance is an indication that unbiased third parties, using the same economic valuation method that will be employed by a bankruptcy court, do not see any substantial equity in the property. The attention focused upon 'workouts' and the growing law of lender liability are but two indications of the fact that lenders do not look at foreclosures as a source of huge profits, but prefer to work with the borrower to put the loan back on a paying basis. The canard of lender windfalls on foreclosure

continues unabated and seems directly to influence supporters of the *Durrett* rule."

(Zinman, at pp. 598-599.)

D. Mortgagees do have incentive to bid at foreclosure sales and almost never receive a double recovery in the form of a deficiency judgment.

BFP Amici argue that a mortgagee has no incentive to bid fair market value and often only bids a nominal amount because he can obtain market value upon resale, resulting in a double recovery, i.e., he obtains the property and can subject the mortgagor to a deficiency judgment. (BFP Amici, p. 46-47). Firstly, California's anti-deficiency rules prohibit a deficiency after a nonjudicial foreclosure. (Code of Civ. Proc. § 580d.) Therefore, the foreclosing beneficiary is limited to taking the security or accepting whatever amount is bid by a successful outside (competitive) bidder in complete satisfaction of the secured obligation. Bidding is encouraged and incentive exists to do this. In a judicial foreclosure, the amount of the deficiency is limited by the fair value of the property. (Code of Civ. Proc. § 726.) Further, the Wechsler[7] study cited by Zinman, *supra*, demonstrates that in only one of ninety-four cases was a deficiency judgment obtained and in that case the judgment was not satisfied. (Wechsler, p. 878.)

---

[7] Wechsler, *Through the Looking Glass: Foreclosure by Sale as De Facto Strict Foreclosure – An Empirical Study of Mortgage Foreclosure and Subsequent Resale*, 70 Cornell L. Rev. 850 (1985).

E. Competitive bidding does exist on properties with sufficient value to warrant such bidding.

BFP Amici argue that historically the typical foreclosure sale has produced very little in the way of competitive bidding, citing Skilton. (BFP Amici, p. 51.) Skilton is a 1942 law review article (post-depression) which can hardly be cited as authority for the effect of current foreclosure laws which have been frequently amended in the past fifty-one years. On the contrary, the Wechsler study shows that competitive bidding exists about 25% of the time and that the remaining sales were probably of properties which were over encumbered, neglected, or abused. (Zinman, at p. 598, fn. 67.)

F. Allowing § 548 set asides will increase the cost of mortgage lending.

BFP Amici assert that there have been no negative effects from *Durrett* and no destabilizing effect on the mortgage market, citing the Shuchman Data. The Zinman Data expresses the doubtful nature of the Shuchman Data's conclusions given its reliance solely on residential mortgage statistics to the exclusion of commercial mortgages; its inconclusive and misleading results; its assumption that mortgage lending officers and their real estate lawyers will react quickly to lower court bankruptcy decisions; and its implicit assumption that the costs and risks of lending do not affect the cost of borrowing and the availability of financing. The Zinman Data article sets forth the reasons for doubt and then his basis for concluding that mortgage lending costs will increase if *Durrett* type decisions are imposed nationwide.

VIII. Billions Of Dollars Of Second Mortgage Capital Would Be Endangered Should Foreclosure Sales Be Subject To Set-Aside For Up To Three Years After They Occur.

The second mortgage market consists in large part of lenders who are private investors often investing savings and retirement funds (e.g., IRA'S and pension plans). Investments by these individuals fund the billions of dollars in loans often to the very borrowers who need money the most (i.e., those with prior credit problems, marginal equity, or a with history of defaults)[8]. These investors invest because of higher returns and expect some higher risks than are involved with high quality, first deeds of trust with institutional lenders. However, a risk of having to defend fraudulent conveyance lawsuits and of having the investment tied up for years will be sufficient to dry up this private money market as private investors will look for a safer place to invest their retirement savings.

CONCLUSION

The well-reasoned thoughts of Professor Zinman are appropriate in closing:

> "[M]ortgage foreclosures are not the demons they are painted to be. The history of the mortgage law has seen a long series of tradeoffs as equity courts and legislatures developed procedures to balance the rights of the lender and borrower. The rules that go into making that balance are not the same in each jurisdiction. It would seem, however, that some reasonable credibility should be given to each state's determination of what that balance should be, given the circumstances that exist in that jurisdiction.

---

[8] It can be concluded from a recent California Department of Real Estate report that mortgage brokered loans in California amounted to over $16,000,000,000.00 in 1990.

> It is not, in any case, the function of the federal Bankruptcy Code to attack collaterally what one does not like in state law. Using the Bankruptcy Code for something it was not intended to do can only result in adverse consequences to the well-ordered administration of bankruptcy and the smooth functioning of the economy of the nation."

(Zinman, *supra*, at p. 603.)

The result sought by Petitioner and BFP Amici would turn on its head over 400 years of precedent interpreting the fraudulent conveyance laws, precedent in the 9th Circuit, and the precedent of logic. They would upset the reasoned balance now existing between the important and carefully crafted policies of the states regarding the enforcement of real property secured liens and the need to protect unsecured creditors from the nefarious activities of their debtors. No solid and corroborated basis for their positions exists in the evidence before the Court. To the contrary, rather than assist unsecured creditors, the result will be to depress foreclosure sale bidding, cloud real property titles for years, and spawn untold needless litigation and bankruptcy filings. The decision of the 9th Circuit Court of Appeals should be affirmed.

Dated: August 20, 1993

Respectfully submitted,

PHILLIP M. ADLESON*
*Counsel of Record

PATRIC J. KELLY
BARBARA B. CHRISTENSEN
DUANE W. SHEWAGA
ADLESON, HESS, CHRISTENSEN & KELLY
110 North Third Street
San Jose, California 95112
(408) 297-6605

Attorneys for Amici Curiae